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Meanwhile a doctrine had received the sanction of the Supreme Court, that intangible property employed in business in a state has a taxable *situs* there. In a series of cases it was held that money deposited in a bank, securities, and credits employed in business in a state not that of the owner's domicile were taxable in the state in which they were employed, having there what has often been called a "business *situs*." ¹¹ Mr. Justice Holmes, indeed, went so far in the case of *Blackstone v. Miller* ¹² as to describe money on deposit as for taxing purposes the same thing as a chattel. ¹³ It may fairly be said, as a result of these cases, that a bank deposit made in a state in the course of and for the use of a business carried on within the state is taxable by the state because it has an actual *situs* there.

A recent decision of the Supreme Court in the case of *Fidelity & Columbia Trust Co. v. Louisville* ¹⁴ has, however, held that the state of domicile of the owner of the deposit might levy a tax upon it, though admitting that the state in which the deposit was made might also tax it. Mr. Justice Holmes said of the decision in *Union Refrigerator Transit Co. v. Kentucky*, *supra*, that "this court has not attempted to press the principle so far."

As a result of this decision it would seem that under no circumstances will the doctrine of *Union Refrigerator Transit Co. v. Kentucky* be applied to a tax on intangible property, whether the property has a business *situs* or is for any other reason under the taxable control of a state other than that of the owner's domicile.

STOCK DIVIDENDS AS INCOME. — "A word is not a crystal, transparent and unchanged, it is the skin of a living thought and may vary greatly according to the circumstances and the time in which it is used." Mr. Justice Holmes thus commented on the fact that a word does not necessarily have the same meaning when used in a statute and in the Constitution. The Supreme Court of the United States was passing on the much-disputed question of whether a stock dividend declared by a corporation on the occasion of transferring a surplus to its capital account is income to the stockholders. This time the question came up, in the case of *Towne v. Eisner*, ¹ under the Income Tax Act of 1913.² That act provided for a tax to be "levied . . . upon the entire net income arising or accruing from all sources . . . to every citizen of the United States." The court held that a stock dividend representing a

¹¹ *New Orleans v. Stempel*, 175 U. S. 309; *Bristol v. Washington County*, 177 U. S. 133; *Metropolitan Life Ins. Co. v. New Orleans*, 205 U. S. 395.

¹² 188 U. S. 189.

¹³ "There is no doubt that the courts in New York and elsewhere have been loath to recognize a distinction for taxing purposes between what commonly is called money in the bank and actual coin in the pocket. The practical similarity more or less has obliterated the legal difference. . . . We shall not stop to discuss this aspect of the case, because we prefer to decide it upon a broader view."

¹⁴ 38 Sup. Ct. Rep. 40. See Recent Cases, page 806.

¹ 38 Sup. Ct. Rep. 158.

² 38 U. S. STAT. 114, 116, 167; COMP. STAT. (1913), § 6319.

surplus earned by the corporation before January 1, 1913, and declared after the passage of the act, was not income to the stockholders within the meaning of the act.

It may be assumed at the outset that the fact that the dividend represented a surplus earned before the passage of the act is not important, and that the court would have held the same had the surplus been earned after the adoption of the act. Nothing in the reasoning of the court turns on that point, and it has been held that income earned before the act was passed but received after the passage is taxable.³ The question, therefore, presented by the decision is the broad one of whether a stock dividend representing the surplus earnings of a corporation is income to the stockholders for the purpose of taxation under the act in question.

The question of the status of a stock dividend as income has most frequently arisen in connection with the distribution of trust property between a life tenant and remainderman, when the settlor has provided that the income from stock left in trust should be paid to the former for life, and thereafter the *corpus* of the stock be turned over to the latter. The determining factor in these cases is, of course, the intention of the settlor, and if the language of the trust indicates what his intention with regard to stock dividends was, that will be decisive. It is the cases, however, where the only expressed intention is contained in the word "income," that cause the trouble, and on this question a number of different rules have arisen in different jurisdictions. It has been held that a stock dividend is never income, and hence never goes to the life tenant;⁴ that it is always income;⁵ or that it is income so far as it is declared out of surplus earned during the life estate, and belonging to the life tenant, but capital so far as it is declared out of surplus earned before the creation of the trust, and belonging to the remainderman.⁶ It would seem that the last is the best rule, for the settlor can hardly

³ *Edwards v. Keith*, 231 Fed. 110; *Southern Pac. Co. v. Lowe*, 238 Fed. 847; *Brusha v. Union Pac. R. R.*, 240 U. S. 1.

In *Trefry v. Putnam*, 116 N. E. 904, 911, 912, the Massachusetts supreme court held, *inter alia*, that both a stock and a cash dividend were taxable when declared after the passage of a statute similar to the federal Income Tax Act, although the surplus was earned before the passage of the statute. But see *Lynch v. Turrish*, 236 Fed. 653. That case can be distinguished in that the dividends were paid out of an increase in the value of capital, and not earnings, prior to January 1, 1913.

⁴ Such is the Massachusetts rule. Cash dividends are income and go to the life tenant, and stock dividends are capital and go to the remainderman. Nothing turns on when the surplus was earned. *Minot v. Paine*, 99 Mass. 101; *Daland v. Williams*, 101 Mass. 571; see *Leland v. Hayden*, 102 Mass. 542.

⁵ Such is the so-called "New York and Kentucky Rule." Both stock and cash dividends go to the life tenant as income, regardless of when the fund out of which they were declared was earned. *Lowry v. Farmers Loan & Trust Co.*, 172 N. Y. 137, 64 N. E. 796; *Hite v. Hite*, 93 Ky. 257, 20 S. W. 778. But New York a few years ago adopted the Pennsylvania rule of apportionment. *In re Osborn*, 209 N. Y. 450, 103 N. E. 723, 823.

⁶ Such is the so-called Pennsylvania rule, in force in the majority of jurisdictions of this country. Stock and cash dividends are treated alike, and are apportioned between life tenant and remainderman. *Earp's Appeal*, 28 Pa. 368.

In England, ordinary dividends, cash or stock, are income, and extraordinary dividends, capital. *In re Barton's Trust*, L. R. 5 Eq. 238.

For a discussion of the law in this country see 16 HARV. L. REV. 54. See also 2 PERRY, TRUSTS, §§ 544, 545; 1 MORAWETZ, PRIVATE CORP., § 468.

be said to have intended to make his gift to the life tenant depend on the policy of the corporation either to divide its earnings as cash, or to reinvest them as capital in the hope of increased earnings in the future; and, therefore, if the corporation decides on the latter policy, it is fair that the life tenant should be compensated by receiving stock equal in value to the surplus earned during the life tenancy. The United States Supreme Court has held, however, in a case arising in the District of Columbia,⁷ that a stock dividend is not income, but belongs to the remainderman.

Admitting, however, that the better rule may be that a stock dividend is income as between life tenant and remainderman, that is neither decisive nor of very great weight on the question whether it is income for the purpose of taxation. The two cases raise entirely different problems. Where trust property is being distributed it is a question of what is fair between two donees who each have an interest in the stock, and of what was the intention of the settlor. Where the Income Tax Act is being interpreted it is a question of depriving a person of property, and of determining the intent of the legislature to make such deprivation. It is a settled rule of construction that a statute imposing a tax is to be interpreted strictly, that the tax must be provided for in clear, unequivocal language, and that all doubts must be construed in favor of the person taxed.⁸ Under such a rule the word "income" must not be given a large, loose meaning.

From this point of view, the decision of the Supreme Court in *Towne v. Eisner*,⁹ that a stock dividend representing surplus earnings transferred to capital is not income to the stockholder, is clearly correct. In so deciding, the court reversed the decision of the Circuit Court of Appeals,¹⁰ and held contrary to the Massachusetts supreme court on the same question arising under a similar statute.¹¹ The reasoning of the Circuit Court of Appeals and of the Massachusetts court is essentially the same. Each court lays stress on the point that, after the issue of the stock dividend, the stockholder has something which he did not have before, that the relation between him and the corporation has changed to his advantage, and that, so far as concerns the accumulation of profits, he now has a permanent interest in the enterprise, whereas before he had merely a right to share in the profits dependent on the discretion of the directors. The federal court argues:¹² "The objection seems impressive that the transaction in no wise affected what the stockholder already had except to give him additional pieces of paper evidencing his ownership. He does, however, have something different before and after receiving the stock. What was before a mere chance that he might receive his share of the surplus in cash dividends and a vague right to secure them if the directors withheld them in a way and to an extent to indicate bad faith is now converted into a permanent interest in the capitalized surplus."

⁷ *Gibbons v. Mahon*, 136 U. S. 549.

⁸ *Mutual Benefit Life Ins. Co. v. Herold*, 198 Fed. 199, 201, citing *Spreckels Sugar Co. v. McLain*, 192 U. S. 397, 416; *Benziger v. United States*, 192 U. S. 38; *United States v. Wigglesworth*, 2 Story, 369.

⁹ *Supra*, note 1.

¹¹ *Trefry v. Putnam*, 116 N. E. 904, 911.

¹⁰ *Towne v. Eisner*, 242 Fed. 702.

¹² 242 Fed. 702, 706.

Let us examine this argument. Before the declaration of the dividend there was no income to the stockholder. The undivided earnings of the corporation were not income to him, for the accumulation of a surplus does not of itself entitle the stockholder to dividends, that being within the discretion of the directors.¹³ The stockholder has only an indirect interest in the corporate property.¹⁴ The fact that the stock rose in value was not income. It merely meant that the chance of receiving income in the form of dividends was becoming more valuable.¹⁵ The issue of a cash dividend would be income for the stockholder, for by the issue his indirect interest in the corporate property would be changed into a direct control over property of his own. No such change takes place when a stock dividend is declared. The corporation parts with no property; it merely changes the label on part of its property for purposes of bookkeeping. The stockholder receives no property; his interest in the corporate assets is identical with what it was before the issue, although evidenced by more shares of stock. This interest is no more vested in the stockholder, no more certain, than before. The corporation has, with one exception, the same control over the property as before, and can exercise the same discretion in the use of the property as before. That exception, as pointed out by the Massachusetts court and the Circuit Court of Appeals, is that dividends may no longer be declared from this fund, for it has become capital. But this change in the powers of the directors is not income to the stockholder, and it actually precludes the possibility of his getting income from the corporation as far as that fund is concerned. The declaration of the stock dividend has perpetuated the corporated control over the property. Such is the reasoning of the United States Supreme Court in the principal case.¹⁶ The Massachusetts court and the Circuit Court of Appeals seem to have failed to grasp the real nature of a stock dividend.¹⁷

The federal Income Tax Act, passed in 1916,¹⁸ provides expressly that stock dividends payable out of corporate earnings should be taxed as income. The effect of the decision of the Circuit Court of Appeals¹⁹

¹³ *New York, etc. Ry. v. Nickals*, 110 U. S. 296; *MORAWETZ, PRIVATE CORP.*, § 276.

¹⁴ *Humphrey v. McKissock*, 140 U. S. 304.

¹⁵ The mere rise in value of stock when there has been no distribution of earnings in the form of dividends is generally held not to be income for the life tenant. *Boardman v. Mansfield*, 79 Conn. 634, 66 Atl. 169; *Tubb v. Fowler*, 118 Tenn. 325, 99 S. W. 988. *A fortiori*, it should not be income for taxation.

¹⁶ *Supra*, note 1.

¹⁷ It is interesting to note that both in Massachusetts and in the federal courts the rule as regards the distribution of trust property is that a stock dividend is not income for the life tenant. *Supra*, notes 4 and 7. The Massachusetts court refused to be bound by the rule, on the ground that it was construing the Massachusetts constitution, and therefore ought to give the word "income" a liberal interpretation. *Trefry v. Putnam*, 116 N. E. 904, 910, 912. The court, however, was first of all construing the statute imposing the tax, where a strict interpretation was in order. The Circuit Court of Appeals distinguished the trust case from the one before it on the ground that in the former the rule was based on convenience of administration of the trust, thus ignoring the principal basis for the decision in the trust case, that a stock dividend was not in fact income. *Supra*, note 7. Moreover, the argument of convenience may be directed only against the rule of apportionment between life tenant and remainderman, and has no weight in deciding between the two remaining alternatives of giving the whole stock dividend to the life tenant or to the remainderman.

¹⁸ *COMP. STAT.* (1916) § 6336 b.

¹⁹ *Supra*, note 11.

was to hold such a provision constitutional under the Sixteenth Amendment.²⁰ In reversing the decision, the Supreme Court merely held that a stock dividend was not income within the meaning of the statute, so that the constitutional question is yet to be decided. The reasoning of the Supreme Court, that a stock dividend is not income, is just as applicable to the constitutional question as it was to the interpretation of the statute. There is, however, a vital difference between the two issues. Not only must the language of the Constitution be given a liberal interpretation as opposed to the strict and narrow construction given the same language in a statute imposing a tax, but there exists also the well-defined policy, often expressed by the courts,²¹ although sometimes not followed,²² that a statute shall not be declared unconstitutional unless it is so beyond a reasonable doubt.²³ Where a coördinate branch of the government has put one interpretation on the Constitution, that interpretation should be upheld by the courts if it is within reason. There is no question but that, when a corporation accumulates a surplus, the stockholder is enriched thereby, although he may have no direct control over those earnings, for the market value of his stock has been increased. If a cash dividend is then declared, the stockholder receives an income which is taxable, and the value of his stock falls in proportion to the amount of the dividend. If a stock dividend is declared, the value of the outstanding stock, the old plus the new, is about the same as it was before the issue. Is it reasonable for Congress to say that by this issue the stockholder, who has been enriched by the prosperity of the corporation, has received an income? Can the tax on the stock dividend be upheld as a tax, in effect, on the rise in value of the securities due to the accumulation of the surplus?²⁴ That is the question on which the Supreme Court must pass.

RIGHT TO DISCONTINUE EMINENT DOMAIN PROCEEDINGS. — There is in every state, in the federal law, and in England some statutory¹ provision controlling the exercise of the power of eminent domain.² However, the statutes very generally fail to go into detail, so a very considerable body of eminent domain law must come from the courts.

²⁰ "The Congress shall have the power to levy and collect taxes on incomes, from whatever sources derived, without apportionment among the several states, and without regard to any census enumeration."

²¹ See the cases cited in THAYER, LEGAL ESSAYS, 13-19.

²² See a Note in the January number of this REVIEW, 31 HARV. L. REV. 475, and an address, cited therein, by Roscoe Pound, TRANSACTIONS, MARYLAND BAR ASSOCIATION (1909), 301.

²³ THAYER, LEGAL ESSAYS, 20-33; COOLEY, CONST. LIMITATIONS, 253-57.

²⁴ It must always be kept in mind that if property is sold at a profit, that is, if the stockholder realizes on this rise in value of his securities by selling them, that profit is taxable as income. COMP. STAT. (1916) § 6336 b [c].

¹ Statute is used throughout this discussion in its broad sense, *i. e.*, as designating the written law as contradistinguished to unwritten law.

² STIMSON, AMERICAN STATUTORY LAW, §§ 90-97 and §§ 1140-49; NICHOLS, EMINENT DOMAIN (2 ed.), § 204; The Lands Consolidation Act, 8 VICT. c. 18 (1845).